Report No. FSD15010	London Borough of Bromley	Agenda Item No.

PART 1 - PUBLIC

Decision Maker:	**Resources Portfolio Holder**		
Date:	**For pre-decision scrutiny by Executive and Resources PDS Committee on 4th February 2015**		
Decision Type:	Non-Urgent	Non-Executive	Non-Key
Title:	**TREASURY MANAGEMENT PERFORMANCE - Q3 2014/15**		
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Chief Officer:	Director of Finance		
Ward:	Alll		

1. Reason for report

1.1 This report summarises treasury management activity during the quarter ended 31st December 2014 and the period 1st April 2014 to 31st December 2014. It also updates Members on the Council's investment with Heritable Bank (paragraph 3.14). The report ensures that the Council is implementing best practice in accordance with the CIPFA Code of Practice for Treasury Management. Investments as at 31st December 2014 totalled £262.5m (excluding the balance of the Heritable investment) and there was no outstanding external borrowing. For information and comparison, the balance of investments stood at £264.9m as at 30th September 2014 and £250.0m as at 31st December 2013 and, at the time of writing this report (23rd January 2015) it stood at £282.4m.

RECOMMENDATION(S)

2.1 The PDS Committee and Portfolio Holder are asked to note the report.

Corporate Policy

1. Policy Status: Existing policy. To maintain appropriate levels of risk, particularly security and liquidity, whilst seeking to achieve the highest rate of return on investments.

2. BBB Priority: Excellent Council.

Financial

1. Cost of proposal: N/A

2. Ongoing costs: N/A.

3. Budget head/performance centre: Interest on balances

4. Total current budget for this head: £1.591m (net interest earnings) in 2014/15; currently forecast to be £1.1m over budget

5. Source of funding: Net investment income

Staff

1. Number of staff (current and additional): 0.25 fte

2. If from existing staff resources, number of staff hours: 9 hours per week

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Legal

1. Legal Requirement: Non-statutory - Government guidance.

2. Call-in: Call-in is applicable

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): n/a

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Ward Councillor Views

1. Have Ward Councillors been asked for comments? N/A.

2. Summary of Ward Councillors comments:

3. COMMENTARY

General

3.1 Under the requirements of the CIPFA Code of Practice on Treasury Management, the Council is required, as a minimum, to approve an annual treasury strategy in advance of the year, a mid-year review report and an annual report following the year comparing actual activity to the strategy. In practice, the Director of Finance has reported quarterly on treasury management activity for many years, as well as reporting the annual strategy before the year and the annual report after the year-end. This report includes details of treasury management activity during the quarter ended 31st December 2014 and the period 1st April 2014 to 31st December 2014. The 2014/15 annual treasury strategy, including the MRP (Minimum Revenue Provision) Policy Statement and prudential indicators, was originally approved by Council in February 2014. Amendments (comprising an increase in the limits for part-nationalised banks, Lloyds and RBS, a lowering of the minimum credit rating for bond investments and the inclusion of diversified growth funds as permitted investments) were approved by Council in October 2014. The annual report for the financial year 2013/14 was approved by the Council in July 2014 and the 2015/16 annual treasury strategy is reported elsewhere on this agenda.

3.2 Recent changes in the regulatory environment place a much greater onus on members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the actual position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

Treasury Performance in the quarter ended 31st December 2014

3.3 **Borrowing:** The Council's healthy cashflow position has continued through the first three quarters of 2014/15, as a result of which no borrowing has been required.

3.4 **Investments:** The following table sets out details of investment activity during the December quarter and during the financial year 2014/15 to date:-

	Qtr ended 31/12/14		**1/4/14 to 31/12/14**	
Main investment portfolio	**Deposits £m**	**Ave Rate %**	**Deposits £m**	**Ave Rate %**
Balance of "core" investments b/f	195.50	1.08	172.00	0.83
New investments made in period	73.00	1.57	211.50	1.22
Investments redeemed in period	-31.00	-0.85	-146.00	0.74
"Core" investments at end of period	237.50	1.18	237.50	1.08
Money Market Funds	0.00	para 3.10	0.00	para 3.10
Svenska Handelsbanken instant access	0.00	para 3.11	0.00	para 3.11
Deutsche Bank 95 day notice	5.00	para 3.11	5.00	para 3.11
CCLA Property Fund	10.00	para 3.13	10.00	para 3.13
Diversified Growth Funds	10.00	para 3.13	10.00	para 3.13
Payden Sterling Reserve Fund	0.00	para 3.12	0.00	para 3.12
Total investments at end of period	**262.50**	**n/a**	**262.50**	**n/a**
Heritable deposit - frozen (para 3.13)			5.00	6.42

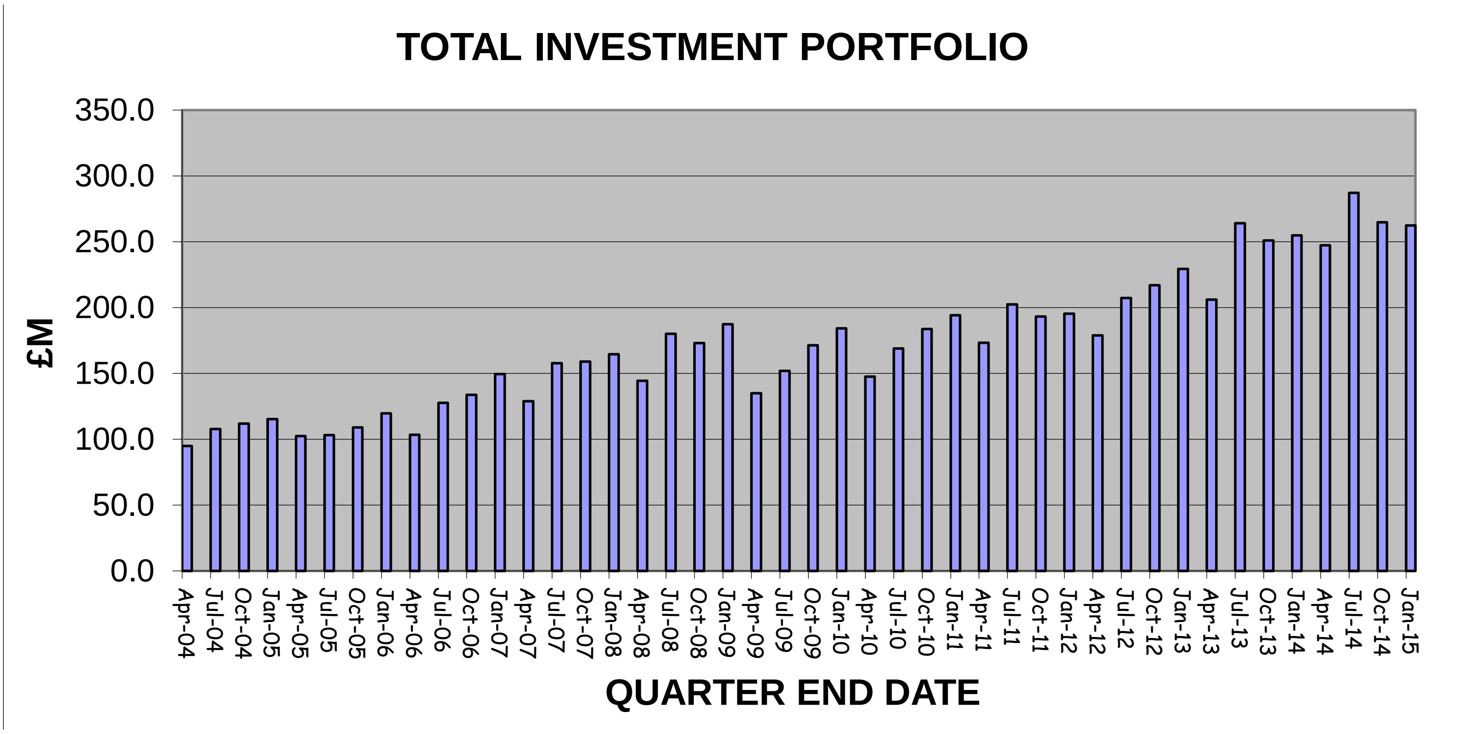
3.5 The following investments were placed in the December quarter:

- Lloyds Bank – fixed term deposits £5m for 1 year @ 1.00% and £25m for 2 years @ 1.09%
- RBS – CD £40m for 3 years @ 1.85%
- Local authorities - £3m for 3 years @ 1.90%
- Diversified Growth Funds - £5m with both Newton and Standard Life

3.6 Details of the outstanding investments at 31st December 2014 are shown in maturity date order in Appendix 1 and by individual counterparty in Appendix 2. An average return of 1% was included for new investments in the 2014/15 budget and the average return on all new "core" investments placed in the December quarter was 1.57%. For comparison, the average LIBID rates for the December quarter were 0.36% for 7 days, 0.43% for 3 months, 0.56% for 6 months and 0.87% for 1 year. The average rate achieved on new investments placed in the period 1st April to 31st December 2014 was 1.22%, compared to the average LIBID rates of 0.35% for 7 days, 0.43% for 3 months, 0.56% for 6 months and 0.88% for 1 year. The improved average rate earned on new investments so far this year mainly reflects longer-term deposits placed with other local authorities and banks and compares favourably with the budget assumption.

3.7 Reports to previous meetings have highlighted the fact that options with regard to the reinvestment of maturing deposits have become seriously limited in recent years following bank credit rating downgrades. Changes to lending limits and eligibility criteria, most recently in October 2014 (an increase of £40m (from £40m to £80m) in the lending limits of both Lloyds and RBS and an increase in the maximum period from 2 years to 3 years) have alleviated this to some extent, but we have still found ourselves in the position of not having many investment options other than placing money with instant access accounts at relatively low interest rates. Active UK banks on our list now comprise only Lloyds, RBS, HSBC, Barclays, Santander UK and Nationwide and all of these have reduced their interest rates significantly in recent years. The Director of Finance will continue to monitor rates and counterparty quality and take account of external advice prior to any investment decisions.

3.8 The graph below shows total investments at quarter-end dates back to 1st April 2004 and shows how available funds have increased steadily over the years. This has been a significant contributor to the over-achievement of investment income against budgeted income in recent years.



Interest Rate Forecast

3.9 Base rate has now been 0.5% since March 2009 and the latest forecast by Capita (in January 2015) is for it to begin to slowly rise from towards the end of 2015. Capita's latest interest rate forecast is shown below, together with their previous forecast, provided in October 2014.

Capita's latest economic forecast is included in the report on the Annual Investment Strategy elsewhere on the agenda.

Date	LATEST FORECAST (Jan 15)					PREVIOUS FORECAST (Oct 14)			
	Base Rate	3 month Libid	6 month Libid	1 year Libid		Base Rate	3 month Libid	6 month Libid	1 year Libid
Mar-15	0.50%	0.50%	0.70%	0.90%		0.50%	0.60%	0.80%	1.00%
Jun-15	0.50%	0.50%	0.70%	1.00%		0.75%	0.80%	1.00%	1.20%
Sep-15	0.50%	0.60%	0.80%	1.10%		0.75%	0.90%	1.10%	1.30%
Dec-15	0.75%	0.80%	1.00%	1.30%		1.00%	1.10%	1.20%	1.40%
Mar-16	0.75%	0.90%	1.10%	1.40%		1.00%	1.30%	1.40%	1.70%
Jun-16	1.00%	1.10%	1.20%	1.50%		1.25%	1.40%	1.50%	1.80%
Sep-16	1.00%	1.10%	1.30%	1.60%		1.25%	1.60%	1.80%	2.10%
Dec-16	1.25%	1.30%	1.50%	1.80%		1.50%	1.90%	2.00%	2.20%
Mar-17	1.25%	1.40%	1.60%	1.90%		1.50%	2.10%	2.20%	2.30%
Jun-17	1.50%	1.50%	1.70%	2.00%		1.75%	2.10%	2.30%	2.40%
Sep-17	1.75%	1.80%	2.00%	2.30%		2.00%	2.30%	2.50%	2.60%
Dec-17	1.75%	1.90%	2.10%	2.40%		2.25%	2.40%	2.70%	2.80%
Mar-18	2.00%	2.10%	2.30%	2.60%		2.50%	2.60%	2.80%	3.00%

Other accounts

3.10 Money Market Funds

The Council currently has 7 AAA-rated Money Market Fund accounts, with Prime Rate, Ignis, Insight, Morgan Stanley, Blackrock, Fidelity and Legal & General, all of which have a maximum investment limit of £15m. In common with market rates for fixed-term investments, interest rates on money market funds have fallen considerably in recent years. The Ignis fund currently offers the best rate (around 0.47%). Although there was no money held in Money Market Funds as at 31st December 2014, the total balance has generally been higher in the last two years than previously as bank credit rating downgrades have continued to restrict counterparty eligibility. In the December quarter, Money Market Funds were withdrawn to part-fund the investment of £40m in RBS and £10m in Diversified Growth Funds. Money Market Funds currently offer the lowest interest of all our eligible investment vehicles with the exception of the Government Debt Management and Deposit Fund (currently 0.25%).

Money Market Fund	**Date Account Opened**	**Actual Balance 31/03/14**	**Actual Balance 30/09/14**	**Actual Balance 30/09/14**	**Ave. Rate Q1, 2 & 3 2014/15**	**Ave. Daily balance Q1, 2 & 3**	**Latest Balance 13/01/15**	**Latest Rate 13/01/15**
		£m	**£m**	**£m**	**%**	**£m**	**£m**	**%**
Prime Rate	15/06/2009	-	14.5	-	0.42	6.5	-	0.45
Ignis	25/01/2010	15.0	9.9	-	0.46	10.9	11.9	0.47
Insight	03/07/2009	4.3	-	-	0.41	6.0	-	0.44
Morgan Stanley	01/11/2012	-	-	-	0.37	0.1	-	0.41
Legal & General	23/08/2012	-	-	-	0.43	5.4	-	0.44
Blackrock	16/09/2009	-	-	-	-	-	-	0.34
Fidelity	20/11/2002	-	-	-	-	-	-	0.38
TOTAL		19.3	24.4	0.0		28.9	11.9	

3.11 Notice Accounts

Svenska Handelsbanken

In August 2013, the Council placed £15m in an instant access account with the Swedish Bank, Svenska Handelsbanken. The account originally paid 0.60%, but the rate was reduced to 0.50%

in July 2014. As investment options were limited and the rate was better than that we were earning on our Money Market Funds, the account was left open until after the Council approved the increased limits for Lloyds and RBS in October. The account was, however, closed on 22nd October 2014 to provide part of the funding for the 3 year CD investment with RBS. The average daily balance in the period 1st April to 22nd October 2014 was £8.5m and an average rate of 0.55% was achieved.

RBS

In March 2013, RBS announced a new 95-day notice account paying a rate of 0.80%. The Council made an initial deposit of £12.5m in March and increased this to £15m in April 2013. The rate was reduced to 0.60% in October 2013 and, in April 2014, RBS informed us that the rate would reduce to 0.30% in August, so notice was given to close the account on 25th August 2014. The average daily balance in the period 1st April to 25th August 2014 was £5.0m and an average rate of 0.65% was achieved.

Deutsche Bank

In November 2013, the Council opened a 95-day notice account with Deutsche Bank. At that time, Deutsche was an eligible counterparty on our lending list with a maximum investment sum of £5m, although a recent credit rating downgrade means it is no longer on the list. Following the downgrade, notice to terminate was given at the end of October and the principal sum plus interest will be returned to us on 2nd February 2015. The average daily balance in the first three quarters of 2014/15 was £3.75m and an average rate of 0.67% was achieved.

3.12 Other investments: Corporate Bonds and Payden Sterling Reserve Fund

At its meeting on 12th November 2012, the Council approved the addition of corporate bonds (minimum credit rating AA-, maximum period 5 years) and the Payden Sterling Reserve Fund to our lending list. On 27th November, following advice from Capita, we made our first investment in a corporate bond, £1.1m with Standard Chartered Bank. The bond matured on 28th April 2014 with a coupon value of 0.70%. In October, the Council agreed to a lowering of the minimum credit rating for corporate bonds to A-, which may provide us with more investment opportunities in the future. In November 2012, £15m was invested in the Payden Fund and that sum remained invested until it was withdrawn in December to part-fund other investments. The average daily balance in the period 1st April to 19th December 2014 was £10.8m. Over the lifetime of the investment (November 2012 to December 2014) an average rate of 0.98% was achieved.

3.13 Pooled Investment Schemes

In September 2013, the Portfolio Holder and Full Council approved the inclusion of collective (pooled) investment schemes as eligible investment vehicles in the Council's Investment Strategy with an overall limit of £25m and a maximum duration of 5 years. Such investment would require the approval of the Director of Finance in consultation with the Resources Portfolio Holder.

CCLA Property Fund

Following consultation between the Director of Finance and the Resources Portfolio Holder, an account was opened in January 2014 with the CCLA Local Authorities' Property Fund and an initial deposit of £5m was made. Following more consultation, a further £5m deposit was made at the end of July 2014. This is viewed as a medium to long-term investment. Dividends are paid quarterly and, to 30th September 2014 (the most recent dividend payment), the investment had returned 5.13% net of fees.

Diversified Growth Funds
In October 2014, the Council approved the inclusion of investment in diversified growth funds in our strategy and, in December, £5m was invested with both Newton and Standard Life. Performance data will be reported in due course.

3.14 Investment with Heritable Bank

Members will be aware from regular updates to the Resources Portfolio Holder and the Executive that the Council had £5m invested with the Heritable Bank, a UK subsidiary of the Icelandic bank, Landsbanki, when it was placed in administration in early-October 2008 at which time our investment was, and still is, frozen. An initial dividend was paid to the Council in July 2009 and, since then, a further 13 dividends have been received. To date, 14 dividend payments have been received (most recently in August 2013) totalling £4,783k (94%) of our total claim (£5,087k), leaving a balance of £304k (6.0%). Council officers and our external advisers remain hopeful of a full recovery and we are awaiting further information from the administrator.

3.15 External Cash Management

External cash managers, Tradition UK Ltd, currently manage £20m of our cash portfolio and provide useful advice and information on treasury management matters. In the first three quarters of 2014/15, Tradition UK achieved a return of 1.24%, which compares with the in-house team rate of 1.22% for new investments placed in the same period. Tradition UK work to the same counterparty list as the Council's in-house team and so have also been constrained by strategy changes approved after the Icelandic Bank crisis and by ratings downgrades in recent years. Details of externally managed funds placed on deposit as at the time of writing this report are shown below.

Bank	Sum	Start Date	Maturity	Period	Rate
Lloyds	£7.5m	18/08/14	18/08/16	2 years	1.28%
RBS	£5.0m	26/08/14	26/08/16	2 years	Min 1.52%; max 2.00% (linked to 3 month Libor)
West Dumbartonshire Council	£2.5m	26/03/14	24/03/17	3 years	1.60%
Perth & Kinross Council	£5m	23/03/14	24/03/17	3 years	1.45%

Regulatory Framework, Risk and Performance

3.16 The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;

- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2009/10);

- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;

- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;

- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;

- Under the Act the CLG has issued Investment Guidance to structure and regulate the Council's investment activities;

- Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8th November 2007.

3.17 The Council has complied with all of the above relevant statutory and regulatory requirements which limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

4. POLICY IMPLICATIONS

4.1 In line with government guidance, the Council's policy is to seek to achieve the highest rate of return on investments whilst maintaining appropriate levels of risk, particularly security and liquidity.

5. FINANCIAL IMPLICATIONS

5.1 A rate of 1% was assumed in the 2014/15 budget for interest on new investments and the budget for net interest earnings was set at £1,591k. Interest rates still show no real sign of increasing and Capita now expect the Bank of England base rate to begin to rise slowly from the end of 2015. There have been no improvements to counterparty credit ratings, which means that the restrictions to investment opportunities that followed ratings downgrades in recent years have still been in place. However, the increases in the limits for the two part-nationalised banks (Lloyds and RBS) approved by the Council in October, together with higher rates from longer-term deals placed with other local authorities, higher average balances than anticipated and the strong performance of the CCLA Property Fund investment, has resulted in a considerable improvement in interest earnings in 2014/15. At this stage, it is estimated that the 2014/15 outturn for interest earnings will be around £1.1m above budget.

Non-Applicable Sections:	Legal and Personnel Implications
Background Documents: (Access via Contact Officer)	CIPFA Code of Practice on Treasury Management CIPFA Prudential Code for Capital Finance in Local Authorities CLG Guidance on Investments External advice from Capita Treasury Solutions